

Memorandum

*Flex your power!
Be energy efficient!*

To: MARTIN TUTTLE
Deputy Director
Planning and Modal Programs

Date: April 29, 2010

File: P1580-0002 (P1191-0070)

From: MARYANN CAMPBELL-SMITH
Chief, External Audits-Local Governments
Audits and Investigations

Subject: Incurred Cost Audit – Metropolitan Transportation Commission

We have audited the costs claimed by and reimbursed to the Metropolitan Transportation Commission (MTC), totaling \$176,071,397, for work performed pursuant to 67 Agreements with the Department of Transportation (Department) from July 13, 2003, to July 13, 2006. The audit was performed to determine whether the costs were adequately supported and in compliance with the Agreement provisions and with State and federal regulations. This audit was performed as a management service to the Department to assist in its fiduciary responsibility to State and federal regulatory agencies. The audit report, including MTC's response, is attached.

Please provide our office with a Department Action Plan related to the audit recommendations within 90 days of this memorandum. We thank you and your staff for their assistance provided during this audit. If you have any questions or need additional information, please contact Teresa Greisen, Audit Manager, at (916) 323-7910, or me at (916) 323-7105.

Attachment

c: See next page.

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P1580-0002 (P1191-0070)
Incurred Cost Audit Metropolitan Transportation Commission
February 2010

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Chief
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Audits and Investigations
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Audit Report

Summary

Audits and Investigations (A&I) audited the costs claimed by the Metropolitan Transportation Commission (MTC), totaling \$176,071,397, for work performed under 67 Agreements with the California Department of Transportation (Department). (See ATTACHMENT I for list of audited Agreements). Based on our audit, we determined that \$165,382,177 of the \$176,071,397 in reimbursed costs was adequately supported and in compliance with the respective Agreement provisions and State and federal regulations. However, \$10,689,220 in reimbursed costs was not adequately supported and in compliance with the Agreement provisions and State and federal regulations. In addition, we determined that MTC's grant management system had deficiencies.

Objectives

The audit was performed to determine whether costs are adequately supported and in compliance with the respective Agreement provisions and State and federal regulations. The audit was performed as a management service to the Department to assist in its fiduciary responsibility to State and federal regulatory agencies.

MTC is responsible for the claimed costs, compliance with applicable Agreement provisions and State and federal regulations, and the adequacy of its financial management system to accumulate and segregate reasonable, allocable, and allowable costs.

Our audit was conducted in accordance with the Standards for Performance Audits set forth in the Government Auditing Standards issued by the Comptroller General of the United States of America. The audit was less in scope than an audit performed for the purpose of expressing an opinion on the financial statements of MTC. Therefore, we did not audit and are not expressing an opinion on MTC's financial statements.

Methodology

The standards require that we plan and perform the audit to obtain reasonable assurance about whether the data and records reviewed are free of material misstatement, as well as material noncompliance with fiscal provisions relative to the Agreements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and records reviewed. An audit also includes assessing the accounting principles used and significant estimates made by MTC, as well as evaluating the overall presentation.

Scope

The scope of the audit was limited to financial and compliance activities related to the above-referenced Agreements. Our audit of MTC's financial management system included interviews of MTC staff necessary to obtaining an understanding of MTC's accounting and internal controls. The audit consisted of an evaluation of compliance with 2 Code of Federal Regulations (CFR), Part 225; 23 CFR, Parts 420 and 450; 48 CFR, Ch. 1, Part 31;

Audit Report

Scope (Continued)

49 CFR, Part 18; the Department's Local Program Procedures (LPP) 04-10; the Department's Local Assistance Procedures Manual; the Department's Regional Planning Handbook; and requirements as stipulated in MTC's Agreements with the Department for the reimbursement of costs totaling \$176,071,397, relating to 67 Agreements open as of July 13, 2003, through July 13, 2006. Our field work was completed on April 16, 2009, and transactions occurring subsequent to this date were not tested, and accordingly, our conclusion does not pertain to costs or credits arising after this date. We believe that our audit provides a reasonable basis for our conclusion.

Because of inherent limitations in any financial management system, misstatements due to error or fraud may occur and not be detected. Also, projections of any evaluation of the financial management system to future periods are subject to the risk that the financial management system may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

Our findings and recommendations take into consideration MTC's response of November 16, 2009, to our June 2009 draft report. An exit conference was held on September 3, 2009, with MTC management personnel. In addition, an exit conference was held on June 25, 2009, with Department and FHWA management personnel. Our Findings and Recommendations, a summarization of MTC's response, and our analysis of the response are set forth in the Findings and Recommendations of this report. A copy of MTC's response is included as ATTACHMENT IV.

Background

MTC was created by the State Legislature in 1970 as the transportation planning, coordinating, and financing agency for the nine-county San Francisco Bay Area. MTC functions as both the regional transportation planning agency and the region's Metropolitan Planning Organization (MPO). For these roles, MTC annually receives various State and federal funds from the Department for transportation and planning-related projects. MTC receives a majority of its federal funds through the Department either indirectly from the Federal Highway Administration (FHWA) or the Federal Transit Administration (FTA). MTC also receives various State funding (i.e., Traffic Congestion Relief and Freeway Service Patrol Funds) from the Department.

The Department's Division of Transportation Planning requested A&I to perform an incurred cost audit of MTC.

Conclusion

Based on our audit, we determined that \$165,382,177 of the \$176,071,397 in reimbursed costs was adequately supported and in compliance with the

Audit Report

Conclusion (Continued)

respective Agreement provisions and State and federal regulations. However, \$10,689,220 in reimbursed costs was not adequately supported and in compliance with the Agreement provisions and State and federal regulations. In addition, we determined that MTC's grant management system had deficiencies. Please refer to the Findings and Recommendations below for further details. (Also see ATTACHMENT II for Schedule of Disallowed Costs.)

This report is intended for the information of MTC, Department Management, the California Transportation Commission, and the FHWA. This report is a matter of public record and will be included on the "Reporting Transparency in Government" website.

If you have any questions, please contact Teresa Greisen, Audit Manager, at (916) 323-7910, or me at (916) 323-7105.

MARYANN CAMPBELL-SMITH
Chief
External Audits – Local Governments
Audits and Investigations
April 16, 2009 (last day of fieldwork)

Audit Report

FINDINGS AND RECOMMENDATIONS

Finding 1 - Project Costs Incurred Prior to E-76 Authorization Dates

The Metropolitan Transportation Commission (MTC) inappropriately billed the California Department of Transportation's (Department) Division of Local Assistance (DLA) \$4,728,470 in project costs incurred prior to the project E-76 authorization dates. These costs were included in 8 of 71 invoices tested. Costs incurred prior to E-76 authorization dates are unallowable for reimbursement. (See ATTACHMENT III for Schedule of Disallowed Invoices.)

Additionally, we found that MTC did not consistently maintain copies of the E-76 forms in the project files. The E-76 forms include critical information and are important documentation to maintain to ensure proper grant management. In order to perform the audit tests, the audit staff had to acquire the missing documents from the Department.

The Department's DLA Agreement 04-6084, Article IV.2 states: *"State and Federal funds will not participate in PROJECT work performed in advance of approval of the 'Authorization to Proceed.'"*

The Department's Local Program Procedures 04-10 states: *"Prior to the beginning of the reimbursable work, the project phase of work eligible for reimbursement from federal funds must be formally authorized (approved) by Caltrans and the Federal Highway Administration (FHWA). The payment of federal funds is limited to the amounts approved on the "Authorization to Proceed" or "E-76." To initiate a federal project authorization for a phase(s) of work, or to increase the authorization for additional phases, the local agency must prepare the "Request for Authorization" package (see Chapter 3 "Project Authorization" of the LAPM) that provides the information needed by Caltrans and FHWA to process the request in a timely manner. Important note: Costs incurred prior to the authorization date are never eligible for FHWA reimbursement except for approved Emergency Relief (ER) work."*

The Special Covenants to the Program Supplements also state: *"Administering Agency agrees that it will only proceed with work authorized for specific phase(s) with an "Authorization to Proceed" and will not proceed with future phase(s) of this project prior to receiving an "Authorization to Proceed" from the STATE for that phase(s) unless no further State or Federal funds are needed for those future phase(s)."*

Audit Report

Finding 1 – (Continued)	49 CFR, Part 18.20(b)(3) states: <i>“Internal Control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes.”</i>
Recommendation	MTC should reimburse the Department \$4,728,470 in project costs incurred prior to the E-76 authorization dates. Additionally, MTC should ensure that copies of all E-76 forms are maintained in the project billing files to assist in proper grant management.
MTC Response	In general, MTC disagrees with the Finding and Recommendation. See ATTACHMENT IV for MTC’s complete response.
Auditor’s Analysis of MTC Response	MTC’s response did not provide any additional documentation to change the Finding and Recommendation of the audit. While MTC concurs that costs were incurred prior to federal authorization dates, MTC contends that the costs should not be disallowed because the funds were properly spent, that the Authorization scope appears to cover an entire fiscal year, and that the Department reviewed and approved invoices. We find no exception to the federal requirement and, accordingly, stand by our Finding and Recommendation.
Finding 2 – Project Costs Billed Before Incurred	<p>MTC violated the Master Agreement provision, which requires that all consultant costs be incurred and paid prior to MTC billing the Department’s DLA. MTC paid the consultants after billing and receiving reimbursement from the Department. Specifically, we found the following:</p> <ul style="list-style-type: none">• MTC inappropriately billed \$3,334,361 of consultant costs to the Department prior to MTC paying the 33 consultants invoices. MTC paid the 33 consultants after receiving reimbursement from the Department. We assessed interest on the consultant invoiced amounts from the date the Department reimbursed MTC to the date MTC paid the consultants. As a result, MTC owes the Department \$11,032 in accrued interest.• MTC inappropriately billed the Department \$1,223,704 for the contract retention portion of 111 consultant invoices prior to MTC paying the consultants. It is MTC’s practice to withhold 3 to 10 percent of project costs (retention) included on consultant invoices until project completion. The practice of withholding a percentage of consultant costs on each invoice is typical of many local agencies; however, the cost should not be billed to the Department until it is actually paid. We found that, even after MTC was reimbursed by the Department, it did not immediately pay the consultants. The average number of days between the dates that the

Audit Report

Finding 2 – (Continued)

Department reimbursed MTC for the consultant retention costs and the date MTC actually paid the consultant was 860 days (or 2.4 years). We assessed interest for each exception based on the actual days outstanding. As a result, MTC owes the Department \$69,963 in accrued interest on consultant retention costs.

Based on the number of instances found, the practice of billing the Department for consultant costs prior to incurring and paying the costs was apparently a standard practice of MTC for the period under audit. This practice is not in compliance with Department Agreements and State and federal regulations. Proper grant management would include ongoing monitoring and establishment of proper internal controls to ensure compliance with Department Agreements and State and federal regulations.

MTC Master Agreements with the Department's DLA stipulate that: *"Administering Agency may submit invoices in arrears for reimbursement of participating project costs on a monthly or quarterly progress basis."*

The Department's DLA, Local Assistance Procedures Manual, Chapter 5.4, states: *"Federal and State law requires that all federal and most State funded local agency project payments be done on a reimbursable basis. Therefore, the local agency must incur the expenditures and pay their contractors prior to invoicing Caltrans for reimbursement of their costs."* Chapter 5.5.14, Format of Invoices, Detailed Invoice Format, states, *"Retention is not eligible for reimbursement until it has been paid to the contractor or deposited into an escrow account."*

49 CFR, Part 18.20(b)(3) states: *"Internal Control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes."*

Recommendation

MTC should pay the Department \$80,995 in accrued interest relating to the Department's loss of earnings on reimbursements made to MTC for consultant costs not yet incurred and paid.

MTC should establish grant management procedures that ensure consultant costs are incurred and paid prior to seeking reimbursement from the Department.

MTC Response

In general, MTC concurred with the Finding and Recommendation. See ATTACHMENT IV for MTC's complete response.

Audit Report

Auditor's Analysis of MTC Response	The finding was revised to omit the \$44,151 disallowed cost because MTC subsequently provided supporting documentation that payment was made to the Consultant in July 2009. The finding was further revised to clarify that the audit finding regarding MTC's payment practices was for the period under audit.
Finding 3 - Improper Procurement Process for Awarding Freeway Service Patrol (FSP) Contracts	<p>MTC improperly awarded 6 consultant procurements for Freeway Service Patrol (FSP). Of the 32 FSP procurements tested, 10 were single-bidder procurements. Of the remaining 22 procurements, MTC improperly awarded six consultant contracts. MTC's procurement process for awarding FSP contracts was not consistent with the criteria set forth in the MTC's Request for Proposals (RFPs). Specifically, the RFPs stated the contracts would be awarded based on criteria of approximate equal weight. However, we found six procurements were awarded in a manner inconsistent with the RFP criteria and panel scoring.</p> <p>There were no documents in the procurement files to support the final awarding decisions. Therefore, the six consultant contracts are unallowable for reimbursement as proper procurement procedures were not followed. The total amount of the six consultant contract procurements was \$4,226,318.</p> <p>49 CFR, Part 18.36(c)(3) states: "<i>Competition – Grantees will have written selection procedures for procurement transactions. These procedures will ensure that all solicitations (i) incorporate a clear and accurate description of all technical requirements for the material, product, or service to be procured.</i>" In addition, MTC's Executive Director Management Memo (EDMM) No. 352 states, <i>1) Evaluation Criteria – Evaluation criteria must be listed in order of importance or if they are of approximate equal weight, this must be communicated to the proposers. 2) Evaluation Procedures – The project manager or panel evaluates each proposal according to the evaluation factors stated in the RFP. A scoring method shall be established by the Project Manager before proposals are received and communicated to the members of the panel.</i>"</p>
Recommendation	MTC should reimburse the Department for the actual expenditures incurred and billed to the Department for the six improperly procured consultant contracts. MTC should establish controls to ensure procurement procedures are consistently followed.
MTC Response	MTC did not concur with the Finding and Recommendation. See ATTACHMENT IV for MTC's complete response.

Audit Report

Auditor's Analysis of MTC Response

We subjected all 32 procurements to the same audit criteria, which included MTC's advertised RFP process. The audit found that 26 of the 32 procurements were awarded consistent with the MTC's advertised RFP process. The remaining 6 procurement awards deviated from MTC's advertised RFP process and the subsequent information provided by MTC did not support that the final award decisions were in compliance.

The Finding and Recommendation remain as written.

Finding 4 - Was Resolved During Draft Process

The draft finding has been removed from the final report since MTC was able to provide adequate supporting documentation.

Finding 5 – Indirect and Unallowable Costs Billed to the Department's Division of Transportation Planning (DOTP) as Direct Costs

MTC incorrectly billed the Department's Division of Transportation Planning (DOTP) \$2,667,763 in indirect and unallowable costs as direct costs. Specifically, we noted that indirect and unallowable costs were included in Work Elements 1111 (Support the Commission), 1154 (Graphics), 1155 (Computer Support), and 1161 (Information Technology Services) in fiscal years (FYs) 2004/05 and 2005/06. Indirect costs incorrectly billed as direct costs included various administrative support costs, such as labor, benefits, travel, and computer support. These costs should have been included in the indirect cost pool and rate to be allocated to all MTC programs. Unallowable costs incorrectly billed as direct costs included the Executive Director's labor, benefits, and travel, as well as the Executive Secretary's time spent on support of MTC Commission meetings.

We restated the indirect rates for both FYs to actual costs and adjusted the indirect cost pool for the incorrect categorizing of costs. We applied the restated rates to the actual direct labor billed for both years to DOTP and determined that DOTP was under-billed \$1,355,591 in indirect costs for both FYs. We offset this amount by the over-billing of direct costs. As a result, the DOTP was over-billed \$1,312,171.

2 CFR, Part 225, Appendix E, section A, states: "*Indirect costs are those that have been incurred for common or joint purposes. These costs benefit more than one cost objective and cannot be readily identified with a particular final cost objective without effort disproportionate to the results achieved.*"

As a result of the restated indirect rates for both FYs, there is no carry-forward to affect future rate calculations for FYs 2006/07 and 2007/08.

Audit Report

Recommendation MTC should reimburse the Department \$1,312,171 in over-billed costs. MTC should ensure only allowable, direct costs are included in Work Elements 1111, 1154, 1155, and 1161, if these Work Elements are to be billed directly to the Department. MTC should routinely review all costs to ensure they are properly categorized.

MTC Response In general, MTC disagrees with the Finding and Recommendation. See ATTACHMENT IV for MTC's complete response.

Auditor's Analysis of MTC Response We reviewed the MTC response and summary document and noted that MTC did not provide a detailed explanation and supporting documentation for adjusting the finding. During the course of the audit, we documented discussions and maintained correspondence with MTC staff regarding the appropriateness of the reclassification of costs in the indirect cost allocation plans for both fiscal years. The documented discussions and correspondence show that MTC agreed to the restated schedules.

While the October 30, 2008, letter from FHWA provided an exception to the federal cost principles for MPO Executive Director's costs, the FHWA decision was not retroactive to prior periods. The Finding and Recommendation remain as written.

**Finding 6 –
Sub-Recipients
Costs Paid and
Billed to the
Department 180
Days After
Agreement
Termination Date**

MTC inappropriately billed the Department's Division of Mass Transportation \$184,934 in sub-recipient costs that were incurred and paid more than 180 days after the termination date of the Department's Agreement. These costs were reimbursed with Traffic Congestion Relief Program (TCRP) funds under Master Agreement 64A0095. The Agreement termination date was June 30, 2004. Per the Agreement, Article I, section 2F states: *"Recipient has 180 days after Termination Date to make already incurred final allowable payments to project contractors or vendors, prepare the Project Closeout Report, and submit the final invoice to State for reimbursement of allowable project costs before those remaining state funds are unencumbered and those funds are reverted as no longer available to pay any project costs. Recipient expressly waives any right to allowable reimbursement for costs incurred after that termination date and for costs invoiced after that 180th day following the project termination date."* The above costs are unallowable because MTC did not incur and bill the costs until well after 180 days beyond the termination date of the Agreement. Specifically, we found the following:

- The Golden Gate Bridge Highway and Transportation District (GGBHTD), a sub-recipient to MTC, billed MTC on May 30, 2004, \$137,035 for various bus parts. MTC did not pay GGBHTD until May 3, 2005, over 180 days after the Agreement termination date of

Audit Report

Finding 6 - (Continued)

June 30, 2004. These costs were included in the final project bill submitted to the Department on November 13, 2007, which was beyond 180 days after the Agreement termination date. As a result, \$137,035 in sub-recipient costs is unallowable, plus \$13,515 in accrued interest, for the period beginning when MTC paid GGBHTD through the date MTC reimbursed the Department the accrued interest on the TCRP funds.

- The San Mateo County Transit District (Samtrans), a sub-recipient of MTC, billed MTC on August 4, 2005, for costs relating to the installation and testing of 13 buses in the amount of \$29,348. MTC reimbursed Samtrans on September 20, 2005, over 180 days after the Agreement termination date of June 30, 2004. These costs were included in the final project bill submitted to the Department on November 13, 2007, which was beyond 180 days after the Agreement termination date. As a result, \$29,348 in vendor costs is unallowable, plus \$2,515 in accrued interest, for the period beginning when MTC paid Samtrans through the date MTC reimbursed the Department the accrued interest on the TCRP funds.
- The City of Vallejo (City), a sub-recipient of MTC, billed MTC on August 23, 2005, \$18,551 for costs relating to vinyl graphics for the sides of buses. MTC reimbursed the City on January 4, 2007, over 180 days after the Agreement termination date of June 30, 2004. These costs were included in the final project bill submitted to the Department on November 13, 2007, which was beyond 180 days after the Agreement termination date. As a result, the \$18,551 in vendor costs is unallowable, plus \$792 in accrued interest, for the period beginning when MTC paid the City through the date MTC reimbursed the Department the accrued interest on the TCRP funds.

Based upon the above, it would appear that MTC did not consistently practice proper grant management. Proper grant management would include ongoing monitoring and establishment of internal controls to ensure compliance with Department Agreements.

49 CFR, Part 18.20(b)(3) states: *"Internal Control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes."*

Audit Report

Recommendation MTC should reimburse the Department \$184,934 in unallowable sub-recipient costs on the advanced TCRP funds. Additionally, MTC should reimburse the Department \$16,822 in accrued interest on the unallowable costs.

MTC should establish grant management procedures that ensure payments to sub-recipients and corresponding Department billings are made on a timely basis and in accordance with Agreement deadlines.

MTC Response MTC did not concur with the Finding and Recommendation. See ATTACHMENT IV for MTC's complete response.

Auditor's Analysis of MTC Response MTC did not provide documentation to support its response. The Finding and Recommendation remain as written.

**Finding 7 –
Lack of Proper
Accountability for
the Advance
Traffic Congestion
Relief Program
(TCRP) Funds**

MTC did not maintain proper accountability for the TCRP funds advanced from the Department's DMT. Specifically, we noted the following:

- MTC did not annually report the interest earned on advanced TCRP funds to the Department. In accordance with the Department's Agreement, MTC was to report annually the interest earned on the daily balance of unused advanced funds for the entire Agreement period and return all accrued interest and the unexpended balance of advanced funds within 30 days of project completion.
- MTC did not reimburse the Department the accrued interest and the unexpended balance of advanced TCRP funds on a timely basis after the termination of the Agreement. In accordance with the Agreement, MTC was to remit the accrued interest and unexpended balance of advanced TCRP funds within 30 days of project completion. MTC reimbursed the Department in two invoices, on June 30, 2007, and October 31, 2007, which was 3 years and 3 years 4 months, respectively, after the project termination date of June 30, 2004.
- In the course of the audit of the TCRP funds, we attempted to verify the accrued interest and remaining balance of outstanding advanced funds. We found that MTC had not routinely and on a timely basis reconciled the general ledger entries of deposits, transfers, withdrawals, and earnings to entries per the bank statements. At our request, MTC performed necessary reconciliations to determine the accrued interest and unexpended balance for the advanced TCRP funds. Without accurate and current reconciling documents, MTC could not determine the correct amount of accrued interest owed and the unexpended balance.

Audit Report

Finding 7 – (Continued)

- MTC did not submit its final bill to the Department until November 13, 2007. In accordance with the Department's Agreement, MTC was to submit its final bill within 180 days from the project termination date of June 30, 2004.

Master Agreement No. 64A0095, section 2B(3) states: *"Interest earned shall be recorded and documented from the time the TCR funds are first deposited in Recipient's account until all the approved TCR advance funds have been expended or returned to State together with all accrued interest. Interest earned shall be reported to State's Project Coordinator on an annual basis and upon final project payment. All interest earned and all unexpended advanced TCR funds shall be returned to state within 30 days of project completion."*

Master Agreement No 64A0095, Article I, section 2F states: *"Recipient has 180 days after Termination Date to make already incurred final allowable payments to project contractors or vendors, prepare the Project Closeout Report, and submit the final invoice to State for reimbursement of allowable project costs before those remaining state funds are unencumbered and those funds are reverted as no longer available to pay any project costs. Recipient expressly waives any right to allowable reimbursement for costs incurred after that termination date and for costs invoiced after that 180th day following the project termination date."*

Based upon the above, MTC did not practice proper grant management. Proper grant management would include ongoing monitoring and establishment of internal controls to ensure compliance with Department Agreements.

49 CFR, Part 18.20(b)(3) states: *"Internal Control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes."*

Recommendation

MTC should implement controls to ensure compliance with Department requirements for reporting and repaying accrued interest on advanced TCRP funds, as well as invoicing final project expenditures.

MTC should ensure that accrued interest amounts are supported with schedules reconciling all related general ledger entries to bank statements and that the reconciliations are routinely performed on a timely basis.

Audit Report

Recommendation (Continued)	MTC should establish grant management procedures that ensure compliance with Department Agreements.
MTC Response	In general, MTC did not concur with the Finding and Recommendation. See ATTACHMENT IV for MTC's complete response.
Auditor's Analysis of MTC Response	MTC did not provide documentation to support its response. The Finding and Recommendation remain as written.
Finding 8 – Final Report of Expenditures Submitted to the Department's DOTP did not Reconcile to Billing Detail	<p>MTC's FYs 2004/05 and 2005/06 Final Report of Expenditures (FROE) do not reconcile to monthly billings submitted to the Department's DOTP; and MTC did not provide explanation and support for the variances.</p> <p>Master Fund Transfer Agreement No. 74A0127, Article 1, section 1K states: <i>"MPO further agrees to ensure that amendments to a previously approved OWP and annual OWPA are adopted by the MPO Board and approved by State, the FTA and FHWA, as applicable, prior to initiating any work identified in those amendments. Changes requiring amendments generally include adding, deleting, or revising a work element; adding funds to, deleting funds from, and /or moving funds between work elements; or revising a scope of work. If a work element or project will not be completed as approved, MPO will report this in its Quarterly Progress Report and amend the OWP/annual OWPA accordingly."</i></p> <p>We compared the monthly billings to the DOTP with the FROE and noted the following:</p> <ul style="list-style-type: none">• For FY 2004/05, MTC reclassified \$126,341 in project labor costs that were originally charged to Work Element 1515 (State Program/Project Monitoring), using MTC Transit Development Act Funds to Federal Highway Administration Planning (FHWA PL) Funds in the FROE. The reclassification of costs between funding sources overran the Work Element 1515 allocation of FHWA PL Funds by \$126,341.• For FY 2005/06, MTC reclassified \$13,169 in Consultant costs that were originally billed to Work Element 1610 (Making the Transportation/Land Use Connection) to Work Element 1110 (Responsible Decision Making Process), and allocated to FTA 5305 Planning Funds in the FROE. The Work Element 1610 had no approved budget for FTA 5305 Planning Funds. These two Work Elements are under separate Mega Work Elements. Per the DOTP Regional Planning Handbook, MTC must seek an amendment to move funding between Mega Work Elements. MTC instead moved costs between Work Elements. Additionally, the budget

Audit Report

Finding 8 – for the Work Element 1110 had been fully expended prior to the
(Continued) reclassification of the costs.

As a result of the variances noted above, these costs are unallowable because MTC did not provide support for the adjustments and/or request approval in accordance with the Master Fund Transfer Agreement.

Recommendation MTC should reimburse the Department \$139,510 in unsupported variances. In addition, MTC should implement the controls necessary to ensure that project costs are billed accurately and any necessary adjustments are reported to the Department in accordance with the Master Fund Transfer Agreement.

MTC Response In general, MTC concurred with the Finding and Recommendation. See ATTACHMENT IV for MTC's complete response.

Auditor's Analysis of MTC Response The finding was revised to omit the \$83,023 disallowance. The revised Finding and Recommendation remain with respect to the two unsupported variances.

Finding 9 – Inappropriate Billing Practices In our audit of the costs billed to the Department's DLA, we found no direct labor costs incurred and charged to projects on 62 of 64 Agreements. The audit found only consultant or sub-recipient costs charged to the Agreements. MTC confirmed that project managers are assigned to projects for the purpose of managing project costs and consultants. However, MTC's job-costing system did not show any project management charges for work performed on DLA projects. MTC stated that project managers responsible for the DLA projects were charged to the DOTP fund sources. This practice is inappropriate because many of the tasks and purposes of the DLA projects are unallowable for use with DOTP funds. Additionally, the practice of charging DLA project management activities to DOTP fund sources does not provide an audit trail to the projects where the activities were performed. Proper grant management procedures would include requiring project managers assigned to manage projects to record the time spent performing these duties directly to the projects.

49 CFR, Part 18.20(6) states: "*Source documentation. Accounting records must be supported by such source documentation as cancelled checks, paid bills, payrolls, time and attendance records, contract and sub-grant award documents, etc.*"

Audit Report

Finding 9 – (Continued)

49 CFR, Part 18.20(b)(3) states: *“Internal Control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes.”*

49 CFR, Part 18.20(a)(2) states: *“Standards for Financial Management Systems...must be sufficient to-permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibition of applicable statutes.”*

Recommendation

MTC should immediately stop charging the DOTP fund sources for project management costs associated with managing DLA projects. MTC should implement proper procedures to ensure that project management charges for DLA projects are accumulated and posted appropriately to corresponding projects in the project costing system.

MTC should determine the labor costs associated with managing the DLA projects that were billed to DOTP fund sources on all DLA projects within the audit universe. MTC should remit the inappropriately billed labor costs to the Department.

MTC Response

In general, MTC concurs with the Finding and Recommendation. See ATTACHMENT IV for MTC's complete response.

Auditor's Analysis of MTC Response

MTC stated that it will review its staffing charges to DOTP funding sources, but did not provide a date by which this review would be completed. We recommend that MTC complete its review within 30 days of the date of this report and provide to the Department a report detailing the results of this review. Any prior labor costs identified as inappropriately billed must be remitted to the Department at this time.

The Department should review the MTC report for accuracy and seek reimbursement for inappropriate labor cost billings.

Finding 10 – Grant Management Deficiencies

MTC's grant management system has deficiencies. There is limited grant compliance oversight as previously noted in Findings 1, 2, 6, 7, and 9 above, and 14 below. In addition, we noted the following:

- MTC did not maintain copies of all Department Master Agreements, Master Fund Transfer Agreements, and Program Supplements. Those that were maintained were not available in a central location for appropriate staff to access. As a result, the appropriate MTC staff were

Audit Report

Finding 10 – (Continued)

unaware of the many compliance requirements relating to each of the Agreements.

- MTC included inaccurate indirect rates and incorrectly labeled costs as “indirect” on its billings to the Department. MTC billings were not sufficiently reviewed prior to submittal to the Department. Without accurate MTC cost reporting, the various Department Programs cannot adequately monitor project costs for compliance in accordance with their Agreements with MTC.
- MTC did not support its project billings with a documented reconciliation to its financial management system. As a result, MTC could not support its review and approval of project costs billed to the Department for reimbursement. Additionally, the project billings were not in compliance with provisions of Department Agreements due to the lack of schedules segregating costs by direct labor, other direct costs, consulting costs, indirect costs, and pass-through costs supporting the billed costs of MTC. In order to perform the audit, we had to request that MTC reconstruct an audit trail from the financial management system to the Department billings in order to support that the costs claimed for each project were appropriate and accurate.
- MTC did not maintain documents in the billing files that reconciled billed project costs to consultant invoices on MTC project billings to the Department’s DLA. Thirty of the 60 supporting consultant invoices tested contain costs for multiple projects, but do not identify the segregation of costs per project. As a result, MTC did not maintain a proper grant management system because they could not demonstrate that Department billings were supported. At our request, MTC reconstructed an audit trail, which documented the flow of costs from consultant invoices through MTC’s financial management system to project billings. While our subsequent review of this newly created documentation did not identify any overbillings, the lack of such documentation increases the risk that overbillings may occur and not be detected.

49 CFR, Part 18.20(b)(3) states: *“Internal Control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes.”* Master Fund Transfer Agreement 74A0127, Article II, section 1, subsection 2 also states, *“MPO shall prepare and submit to State, not more frequently than once a month, but at least quarterly, two signed Requests for Reimbursements of actual allowable costs incurred by MPO consistent with work elements described in the OWP (conforming to the format provided in*

Audit Report

Finding 10 – (Continued)

Appendix B) and including all required information, as applicable, provided for in example Appendix B2 to this MFTA for the reimbursement of actual allowable costs incurred and paid by MPO consistent with work elements described in the OWP.”

Recommendation

MTC should maintain a proper grant management system to ensure compliance with the various provisions stipulated in the Department Master Agreements, the Master Fund Transfer Agreements, and the Program Supplements. Such a system would include maintaining copies of all Agreements, preparing Department billings accurately and in accordance with Agreement requirements. In addition, MTC should maintain billing files with appropriate support that demonstrates the review and approval of all billed project costs.

MTC should develop documentation that reconciles Department billings to consultant invoice costs and maintain this documentation in MTC’s billing files.

MTC Response

In general, MTC did not concur with the Finding and Recommendation. See ATTACHMENT IV for MTC’s complete response.

Auditor’s Analysis of MTC Response

MTC did not provide documentation to support its response. The Finding and Recommendation remain as written.

Finding 11 - Inadequate Internal Controls Over Federal and State Grants

MTC lacks adequate internal controls necessary to maintain proper accountability over its State and federal grants. 49 CFR, Part 18.20(b)(3) states: *“Internal Control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes.”* Specifically, we identified the following issues:

- **Lack of proper invoice approval**

We noted many instances where MTC did not have evidence to support its management review and approval of consultant and pass-through agency invoices. The lack of proper management review and approval of invoices increases the risk for errors and irregularities to occur and go undetected. Additionally, the lack of proper management review and approval of invoices increases the risk that the invoices could include unsupported and/or erroneous charges.

Specifically, we found the following:

Audit Report

Finding 11 – (Continued)

- ❖ Sixty-four of 232 consultant and pass-through agency invoices billed to the Department's DLA (28 percent of invoices tested) lacked evidence of management review and approval.
- ❖ Twenty-four of 60 consultant invoices billed to the Department's DMT (40 percent of invoices tested) lacked evidence of management review and approval.
- ❖ Two of six pass-through agency invoices billed to the Department's DOTP (33 percent of invoices tested) lacked evidence of management review and approval.
- ❖ Four of 71 MTC invoices billed to and paid by the Department's DLA appeared to have the Chief Financial Officer's (CFO) signature of approval. However, upon further review and discussion with MTC staff, we determined that the signatures were made by the Senior Accountant. The Senior Accountant was not authorized to review and approve invoices and did not have authority to sign as the CFO. Therefore, there was no proper management review and approval of the billed costs to the Department.

MTC has policies and procedures for the approval of contract invoices under Executive Director Management Memo (EDMM) No. 352 that states: *"Invoices are sent directly to the Accounting Section under the terms of the contract. Accounting staff attaches a form to be completed by the Project Manager and signed by the Section Manager."* MTC has not implemented the controls necessary to ensure the practice of these policies and procedures.

- **Inadequate controls over access rights**

MTC's Finance Department practices job rotation to cross-train its employees. However, after the rotation of staff, MTC has not removed the former staff's financial management system access rights that were used for previous job duties. As a result, inadequate segregation of duties can occur.

- **No Accounting Manual**

MTC's Finance Department does not have an Accounting Manual. As a result, MTC's ability to consistently practice and process accounting transactions and procedures uniformly is at risk. Additionally, there is an increased risk for errors and irregularities to occur when proper accounting practices and procedures are not formally documented for staff performing the duties within the Finance Department.

Audit Report

- Recommendation**
- MTC should implement the internal controls necessary to ensure contract invoice approval procedures are practiced in accordance with its own policies and procedures and in compliance with requirements as stipulated in 49 CFR, Part 18.
 - MTC should implement the necessary controls to ensure that individuals signing billing invoices on behalf of the CFO are authorized to do so and that the signature clearly indicates that the individual is signing “for” the CFO.
 - MTC should ensure that Finance Department employees assigned new jobs, as a result of job rotation, have their previous financial management system access rights deleted to avoid inadequate segregation of duties.
 - MTC’s Finance Department should create and maintain an Accounting Procedures and Practices Manual.

MTC Response In general, MTC concurred with the Finding and Recommendation. See ATTACHMENT IV for MTC’s complete response.

Auditor’s Analysis of MTC Response The Finding and Recommendation remain as written.

- Finding 12 – Interagency Agreements Lack Required Agreement Provisions**
- MTC’s Interagency Agreements with its pass-through agencies lack required fiscal provisions. Specifically, we found the following:
- MTC’s Interagency Agreements with Santa Clara Valley Transportation Authority (SCVTA), the San Francisco Transportation Authority (SFTA), and the Association of Bay Area Governments (ABAG) do not include the fiscal provisions requiring an accounting system adequate to accumulate and segregate reasonable, allowable, and allocable project costs and the provisions for travel and subsistence costs.
 - MTC’s Interagency Agreements with pass-through agencies of Congestion Management Grants do not include the fiscal provisions requiring an accounting system adequate to accumulate and segregate reasonable, allowable, and allocable project costs, the provisions for travel and subsistence costs, and compliance with the cost principles applicable to consultants, 48 CFR, Chapter 1, Part 31. Additionally, the Right-to-Audit provision should be revised to allow access by the State.

Department DOTP Agreement #MTCMFTA, Section 1, Part 10, states: *“MPO and its subcontractors shall establish and maintain an accounting*

Audit Report

Finding 12 – (Continued)

system conforming to Generally Accepted Accounting Principles (GAAP) to support reimbursement payment vouchers or invoices which segregate and accumulate the costs of OWP work elements by line item and produce monthly reports which clearly identify reimbursable costs, matching costs, and other expenditures by MPO."

Department DOTP Agreement #MTCMFTA, Section 1, Part 14, states in part: *"MPO and its sub-contractors shall invoice STATE for OWP related travel, per diem and subsistence costs at rates not exceeding those authorized to be paid to regular State employees under those rules and regulations of the State Department of Personnel Administration..."*

Department DLA Agreement 04-6084, Article I.6, states in part: *"Administering Agency shall conform to all State statutes, regulations and procedures (including those set forth in LPP 95-07, "Reengineering"[became the Local Assistance Procedures Manual], and subsequent approved revisions and Local Programs Manual updates,...) relating to the Federal-aid Program, all Title 23 Federal requirements, and all applicable Federal laws, regulation, and policy and procedural or instructional memoranda, unless designated in the approved PROGRAM SUPPLEMENT."*

Department DLA Agreement 04-6084, Article V.1, states in part: *"Administering Agency and any third party under contract with Administering Agency shall retain all original records to the project financed with Federal funds and shall make records available upon request by Federal and State representatives."*

The Department's Agreements with MTC require that all pertinent fiscal provisions be included in MTC's Agreements with its pass-through agencies. The lack of adequate fiscal provisions in MTC's pass-through agreements increases the risk of unallowable costs and can result in MTC being unable to recover unallowable costs.

Recommendation

MTC's Interagency Agreements with SCVTA, SFTA and ABAG should include the following fiscal provisions:

- **Accounting System:** "Agency shall establish and maintain an accounting system conforming to GAAP that is adequate to accumulate and segregate reasonable, allowable, and allocable project costs."
- **Travel and Subsistence Costs:** "Reimbursement of Agency travel expenses and per diem rates are not to exceed the rate specified by the State of California Department of Personnel Administration for similar employees (i.e., non-represented employees)."

Audit Report

Finding 12 – (Continued)

MTC's Interagency Agreements with pass-through agencies of Congestion Management Grants should include the following provisions:

- **Accounting system:** "Agency shall establish and maintain an accounting system conforming to GAAG that is adequate to accumulate and segregate reasonable, allowable, and allocable project costs."
- **Travel Per Diems and Subsistence Costs:** "Reimbursement of Agency travel expenses and per diem rates are not to exceed the rates specified by the State of California Department of Personnel Administration for similar employees (i.e., non-represented employees)."
- **Administrative Requirements** to include: "All sub-consultants agree to comply with 48 CFR, Chapter 1, Part 31, Contract Cost Principles and Procedures."

Right to Audit: "Agency shall permit authorized representatives of DOT, the Comptroller General of the US, FHWA, **the State**, and MTC to inspect and audit all data and records relating to Agency's performance under this Agreement including data and records pertaining to subcontracts over \$25,000."

MTC Response

MTC has reviewed its Agreements and believe they are generally in compliance. See ATTACHMENT IV for MTC's complete response.

Auditor's Analysis of MTC Response

Additional language was added to the Finding and Recommendation to provide clarity. It is in the best interest of MTC to have the most current and appropriate language in its Interagency Agreements to ensure recourse from its pass-through agencies.

Finding 13 - Consultant Contracts Lack Required Fiscal Provisions

MTC's consultant contracts lack required fiscal provisions. Specifically, we found the following:

- Thirty-seven of 40 MTC consultant contracts tested did not include provisions requiring compliance to federal cost principles, 48 CFR, Chapter 1, Part 31.
- Thirty-seven of 40 MTC consultant contracts tested did not include reference in the Right-to Audit provision to allow State access.

Audit Report

Finding 13 – (Continued)

The Department's DLA Master Agreement 04-000618, section 15 states: *"The Administering Agency agrees that a reference to either, OMB A-87 or the 48 (Sic) CFR, Chapter 1, Part 31, whichever is applicable and 49 CFR, Part 18 will be included in any subcontracts entered into as a result of this Agreement."*

The lack of adequate fiscal provisions in MTC's consultant contracts increases the risk of unallowable costs and can result in MTC being unable to recover unallowable costs from consultants.

Recommendation

MTC should ensure all consultant contracts include appropriate fiscal provisions as required in the Department's Agreements.

MTC Response

MTC has reviewed contract requirements and believes they are in compliance. However, additional wording will be added for clarity.

Auditor's Analysis of MTC Response

The Finding and Recommendation remain because it is in the best interest of MTC to have all appropriate language in its consultant contracts.

Finding 14 - Incorrect Overall Work Plan (OWP) Work Element Descriptions

MTC's OWP for both FY 2004/05 and FY 2005/06 includes outdated and inaccurate language describing the objectives and tasks for Work Elements 1111 and 1154. The language describing the objectives and tasks for Work Elements 1111 and 1154 is not consistent with the actual costs charged to the Work Elements and does not agree to the MTC budgets for either year. Proper grant management would include reviewing the OWP for current and accurate language describing the objectives and tasks for all Work Elements to ensure the OWP represents an accurate scope of work for transportation planning activities in a given fiscal year. In addition, proper grant management would include ensuring the OWP projected scope of work agrees to the MTC budget. Master Fund Transfer Agreement 74A0127, Article 1, section I states, *"Only work performed during the term of, and consistent with, the work elements in the OWP may be reimbursed."*

Outdated and inaccurate language in the OWP impacts the Department's ability to properly monitor MTC's Work Element objectives and tasks.

Recommendation

MTC should implement grant management procedures to ensure the accuracy of the descriptions for the objectives and tasks of all Work Elements included in the OWP and should include procedures to review and reconcile the OWP Work Element descriptions to the objectives and tasks included in MTC's budget.

Audit Report

MTC Response	In general, MTC did not concur with the Finding and Recommendation. See ATTACHMENT IV for MTC's complete response.
Auditor's Analysis of MTC Response	The finding resulted from the review of internal MTC documents, such as accounting reports of actual expenditures, and budget documents that included budgeted costs for the two Work Elements that do not agree to the language included in the OWP. Federal and State funding partners reviewing the OWP would not have internal documents. The Finding and Recommendation remain as written.
Audit Team	MaryAnn Campbell-Smith, Chief, External Audits – Local Governments Teresa Greisen, Audit Manager Alice Lee, Auditor

MTC
INCURRED COST AUDIT
ATTACHMENT I

LIST OF AUDITED AGREEMENTS

Project Number	Contract No.	Amount Paid by Department
1 Project: STPCML 6084 (095)	Contract: 04-6084-M066	1,355,821
2 Project: CML 6084 (080)	Contract: 04-6084-M057	4,095,230
3 Project: CML 6084 (058)	Contract: 04-6084-M047	7,730,000
4 Project: STPL 6084 (079)	Contract: 04-6084-M063	6,000,000
5 Project: FSP 02-6160 (005)	Contract: 04-6160-M	5,856,814
6 Project: CMLN 6160 (006)	Contract: 04-6160-M00	5,518,100
7 Project: CML 6084 (061)	Contract: 04-6084-M058	5,314,117
8 Project: STPL 6084 (091)	Contract: 04-6084-M074	4,849,810
9 Project: STPL 6084 (083)	Contract: 04-6084-M056	4,953,000
10 Project: FSP04 6160 008	Contract: FSP 04-6160-001	4,871,042
11 Project: CML 6084 (077)	Contract: 04-6084-M055	4,757,911
12 Project: FSP05 6160 009	Contract: FSP05-6160(001)	4,793,928
13 Project: CML 6084 (045)	Contract: 04-6084-M034	4,780,000
14 Project: FSP06-6160 (011)	Contract: FSP06-6160-011	4,742,695
15 Project: STPL 6084 (111)	Contract: 04-6084-M081	2,177,050
16 Project: STPL 6084 (101)	Contract: 04-6084-M076	3,801,178
17 Project: CML 6084 (057)	Contract: 04-6084-M043	3,632,000
18 Project: CML 6084 (082)	Contract: 04-6084-M067	180,485
19 Project: STPL 6084 (110)	Contract: 04-6084-M078	72,042
20 Project: CML 6084 (047)	Contract: 04-6084-M031	3,463,000
21 Project: CML 6084 (103)	Contract: 04-6084-M079	791,265
22 Project: TCRP-04A1(266)	Contract: 04A1 (266)	3,119,300
23 Project: STPL 6084 (071)	Contract: 04-6084-M050	2,923,500
24 Project: STPCML 6084 (107)	Contract: 04-6084-M084	456,267
25 Project: CML 6084 (088)	Contract: 04-6084-M072	1,080,557
26 Project: STPL 6084 (104)	Contract: 04-6084-M085	123,517
27 Project: STPL 6084 (053)	Contract: 04-6084-M	1,758,500
28 Project: STPL 6084 (039)	Contract: 04-6084-M030	1,758,500
29 Project: ACSTPCML-6084 (087)	Contract: 04-6084-M059	1,353,006
30 Project: STPCML 6084(097)	Contract: 04-6084-M071	689,241
31 Project: CML 6084 (078)	Contract: 04-6084-M065	143,075
32 Project: CMLN 6160 (003)	Contract: 04-6160-M002	5,758,267
33 Project: CML 6084 (105)	Contract: 04-6084-M082	60,000
34 Project: RPL 6084 (066)	Contract: 04-0618-857	1,155,000
35 Project: CML-6160 (004)	Contract: 04-6160-M003	5,548,000
36 Project: STPL 6084 (090)	Contract: 04-6084-M075	722,935
37 Project: RPL 6084 (055)	Contract: 04-0618-857	719,000
38 Project: STPL 6084 (081)	Contract: 04-6084-M060	700,000
39 Project: STPL 6084 (085)	Contract: 04-6084-M061	686,000
40 Project: STPL 6084 (098)	Contract: 04-6084-M070	484,496
41 Project: CML 6084 (089)	Contract: 04-6084-M073	51,592
42 Project: CML 6084 (108)	Contract: 04-6084-M080	109,622
43 Project: STPL 6084 (069)	Contract: 04-6084-M048	500,000
44 Project: CML 6084 (080)	Contract: 04-6084-M062	434,295
45 Project: DEM115L 6084 (102)	Contract: 04-6084-M077-R1	500,000
46 Project: STPL 6084 (059)	Contract: 04-6084-M054	500,000
47 Project: STPL 6084 (094)	Contract: 04-6084-M064	111,451
48 Project: STPL 6084 (099)	Contract: 04-6084-M069	16,692
49 Project: STPL 6084 (064)	Contract: 04-6084-M045	423,910
50 Project: PPM 03-6084 (065)	Contract: PPM03-6084 (001)	421,000
51 Project: PPM02-6084 (056)	Contract: PPM02-6084 (001)	420,000
52 Project: PPM01 6084 048	Contract: PPM01-6084- (001)	419,000
53 Project: CML 6084 (050)	Contract: 04-6084-M040	400,000
54 Project: CML 6084 (063)	Contract: 04-6084-M044	399,980
55 Project: STPL 6084 (100)	Contract: 04-6084-M068	81,093
56 Project: VPPL 6084 032	Contract: 04-6084-M026	248,156
57 Project: CML 6084 (042)	Contract: 04-6084-M032	221,000
58 Project: CML 6084 (052)	Contract: 04-6084-M039	221,000
59 Project: CML 6084 (068)	Contract: 04-6084-M052	221,000
60 Project: STPL 6084 (067)	Contract: 04-6084-M049	178,919
61 Project: STPLEE 6249 (008)	Contract: 04-6249-M	99,999
62 Project: ITS 03-6084 (072)	Contract: 04-6084-M053	50,000
63 Project: CML 6084 (114)	Contract: 04-6084-M083	25,000
64 Project: STPL 6084 (070)	Contract: 04-6084-	452,451
65 TCRP 04A0095	Contract: 64A0095	39,861,345
66 FY 04/05 OWP	FY 04/05 OWPA	7,221,758
67 FY 05/06 OWP	FY 05/06 OWPA	9,517,685
Total Audit Population		176,071,397

MTC
INCURRED COST AUDIT
ATTACHMENT II

TOTAL DISALLOWED COSTS

Finding No.	Finding Description	Program (A)	Federal	State	Total Disallowed Cost
1	Costs Incurred Prior to E-76 Dates	DLA	\$ 4,728,470		\$ 4,728,470
2	Project Costs Billed Before Incurred	DLA	\$ 80,995		\$ 80,995
3	Improper Procurements (6)	DLA	(C)	\$ 4,226,318	\$ 4,226,318 (B)
5	Overbilling of Costs to DOTP	DOTP	\$ 1,312,171		\$ 1,312,171
6	Sub-Recipient Costs Billed 180 Days After Agreement Termination Date	DMT		\$ 201,756	\$ 201,756
8	Variance Between FROE and Billings to DOTP	DOTP	\$ 139,510		\$ 139,510
Total Disallowed Costs			\$ 6,261,146	\$ 4,428,074	\$ 10,689,220

(A) Key:

DLA - Division of Local Assistance
DOTP - Division of Transportation Planning
DMT - Division of Mass Transportation

(B) This amount represents the total amount of the procurements. MTC will need to determine the actual expenditures incurred and billed to the Department for the six disallowed procurements and remit that amount to the Department.

(C) During the period of the audit, two of five of the FSP agreements with MTC were partially federally funded. MTC will need to identify which FSP agreements the disallowed procurements were billed.

MTC
INCURRED COST AUDIT
ATTACHMENT III
FINDING 1 - COSTS INCURRED PRIOR TO E-76

Department Contract No.	MTC Invoice No.	Consultant/Subregion Invoiced Amount	Subtotal by Invoice	Total by Contract
CML 6084-058	Invoice #1	556,593		
		323,899		
		525,284	1,405,776	
	Invoice #2	565,718		
		1,026,382	<u>1,592,100</u>	\$ 2,997,876.00
STPL 6084-083	Invoice #1	180,541		
		195,000	375,541	
	Invoice #2	153,324		
		480,626	<u>633,950</u>	\$ 1,009,491.00
CML 6084-077	Invoice #1	134,190	<u>134,190</u>	\$ 134,190.00
STPL 6084-101	Invoice #4	97,500	<u>97,500</u>	\$ 97,500.00
STPL 6084-071	Invoice #1	141,372		
		66,769		
		94,659		
		35,000	337,800	
	Invoice #2	112,863		
		38,750	<u>151,613</u>	\$ 489,413.00
Grand Total Disallowed				<u>\$ 4,728,470.00</u>

ATTACHMENT IV

**METROPOLITAN TRANSPORTATION COMMISSION (MTC)
RESPONSE TO DRAFT AUDIT REPORT**



METROPOLITAN
TRANSPORTATION
COMMISSION

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November 16, 2009

Scott Haggerty, Chair
Alameda County

Adrienne J. Tissier, Vice Chair
San Mateo County

Tom Azarbrado
U.S. Department of Housing
and Urban Development

Tom Bates
Cities of Alameda County

Dennis J. Chin
Cities of Santa Clara County

Dave Cortese
Association of Bay Area Governments

Chris Daly
City and County of San Francisco

Bill Dodd
Napa County and Cities

Dorene M. Giacomini
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Sue Lampert
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Ms. MaryAnn Campbell-Smith, Chief
State of California
Department of Transportation
Audits and Investigations
1304 O Street, Suite 200 (MS 2)
Sacramento, CA 95814

Re: Incurred Cost Audit
Metropolitan Transportation Commission
June 2009

Dear Ms. Campbell-Smith:

Below is the formal response to the draft audit findings report dated June 2009. MTC staff appreciates our being granted the time to complete the 2009 financial close, audit and financial reporting process before responding to the draft audit.

MTC believes that the findings and conclusions in the report, specifically, the conclusion that MTC "does not have an adequate grant management system" ignores a number of mitigating and supporting facts that, when taken into consideration, would reduce the "questioned costs" to a minor level.

- Over the two-year span of field work, MTC staff consistently provided detailed responses to inquiries dating back as far as a decade. Based on our review of Caltrans' invoices to BATA, Caltrans itself only maintains detailed records for five years from the date of the expenditure, not the end of the project. As such, MTC is held to a standard Caltrans itself does not meet.
- During field work, MTC staff pulled over 600 checks without any exception, save for the fact that older inquiries required more outside and off-site research and some supporting information was rejected.
- Questions related to timing of approvals and invoices do not involve questions of compliance with laws, regulations and provisions of contracts directly related to the appropriateness of the expenditures as certified under audit guidelines of A-133.
- MTC has successfully delivered over \$176 million in federally and state funded programs without a single questioned cost determined under the A-133 audit standards.
- Caltrans project and finance staff approved all of the invoices and costs in question. Every invoice and indirect cost support has been reviewed and approved, not just by local staff, but by Caltrans accounting group as well.
- Many of the audit issues (Finding #2) were corrected well in advance of Caltrans field work, including invoicing for reimbursement prior to actual payment, timing of retention payments, as well as start dates for billing under E-76 agreements.

- MTC has provided support for all questioned costs in Finding #4.
- MTC believes the procurement in Finding #3 was properly conducted, reviewed, disclosed and approved.

Finally, MTC believes that the jump to "Disallowed" is excessive given there has been no findings of fraud, waste, abuse, illegal acts, or funds inappropriately spent.

Conclusion:

MTC maintains the highest standards of financial reporting and management. MTC has relied in good faith on the fact that Caltrans project and finance staff have received and approved all of the budgets, costs and expenses that are questioned in this report. As such, we respectfully request the costs for Finding one be reinstated; Findings three and four be removed entirely; and the balance of the costs be revised based on attached information. We further request that the findings and conclusions be revised to more accurately reflect MTC's efforts.

Sincerely,

~~Brian Mayhew, CFO~~
Metropolitan Transportation Commission

BM/cj

Summary of Findings:

<u>Finding</u>	<u>Caltrans Assessment</u>	<u>MTC Assessment</u>	<u>Comment</u>
Finding #1	\$ 4,728,470	Reinstate	<ul style="list-style-type: none"> ▪ Funds were properly spent ▪ Authorization "Date" covered entire fiscal year ▪ Caltrans reviewed and approved invoices
Finding #2	\$ 125,146	\$ 80,995	<ul style="list-style-type: none"> ▪ \$44,151 paid in 2009 ▪ Other process corrected prior to audit
Finding #3	\$ 4,226,318	-0-	<ul style="list-style-type: none"> ▪ Procurement was properly conducted, finding should be removed
Finding #4	\$ 3,062,022	-0-	<ul style="list-style-type: none"> ▪ All support has been reconfirmed, finding should be removed
Finding #5	\$ 1,312,171	\$ 91,153	<ul style="list-style-type: none"> ▪ Executive Director allowable; balance appropriately redistributed
Finding #6	\$ 201,756	Reinstate	<ul style="list-style-type: none"> ▪ Delay was verbally authorized ▪ MTC closed and paid interest
Finding #8	\$ <u>222,533</u>	<u>-0-</u>	<ul style="list-style-type: none"> ▪ \$83,023 finding in error ▪ Remaining funds were adequate to cover expenses
	<u>\$13,878,416</u>	<u>\$ 172,148</u>	

Finding #1 (\$4,728,470):

MTC improperly billed \$4,728,470 in project costs incurred prior to the project E-76 authorization dates.

MTC concurs that the invoices in question involved work authorized prior to receiving the signed E-76. However, we do not concur that MTC proceeded to “future phases” without authorization. As such, we request that Caltrans waive all disallowed amounts.

All five E-76 agreements in question cover operating programs that do not lend themselves to clear breaks between fiscal years. As such, our understanding was that the “Date” on the E-76 covered the entire fiscal year. This was a long-standing practice that is backed up by the fact that invoices were all processed and paid by Caltrans consistent with our understanding

We also submit the following:

- There are several dates on each E-76, including one appearing to cover the fiscal year, which creates the confusion over which is the true effective date.
- There is an authorization/agreement date but the single “Date” on the agreement always appears to cover an entire fiscal year, which is critical for on-going program management.
- The special covenants addressed restrictions on “future phases” and would not apply if the agreement actually covers continuation of the existing phase or operational programs. In fact, all of the agreements covered are for Preliminary Engineering, therefore, MTC never started a future phase without prior authorization
- The E-76 agreements in questions cover operational areas, not changes in project phases:
 - 2001/02 – On-going TravInfo program.
 - 2001/02 – On-going TravInfo program.
 - 2003/04 – CMA Planning Grant. Note here that MTC received the first letter specifying future funding would be lost if we “proceed to future phases prior to obtaining an authorization to proceed for that phase”. The letter applied only to work in “future” phases and does not preclude retroactive authorization.
 - 2003/04 – Regional Rideshare, an ongoing transit program. Note, this is the first time the Notice-to-Proceed letter specifically notes the effective date and warns that work prior to approval is not reimbursable.
 - 2003/04 – On-going CMA planning activities. Note, no restrictive authorizing letter.
 - 2004/05 – On-going CMA planning activities. Note, no restrictive authorizing letter.
- There are 6 E-76 agreements in question that should be carefully evaluated for intent and results rather than administrative process:
 - All expenditures were properly incurred and accounted for under the A-133 process.

- All of the programs are on-going operational programs where expenses cannot easily be placed on hold between agreement years.
- MTC staff relied on the fiscal year to "Date" and while invoices included work authorized prior to the "Agreement Date", it was authorized in the fiscal year covered by the agreement and paid only after receipt of the written agreement.
- All costs were reviewed and approved by the District and paid by headquarters accounting.

Overall, MTC staff was not presented with documentation that authorization had to be written and, given the nature of the projects in question, believed they acted in good faith and in accordance with guidelines. Given the fact that these expenses were properly submitted, reviewed, approved and paid only reinforces the belief that MTC staff acted properly. As such, MTC respectfully requests all disallowed costs be reinstated.

Finding #2 (\$125,146):

MTC received reimbursement prior to paying certain invoices and failed to pay one invoice completely.

\$11,032	Interest on 33 consultant invoices paid after receiving reimbursement.
\$69,963	Interest on 111 contract retention payments billed but not paid.
\$44,151	Reimbursed but unpaid.

MTC concurs that delaying payment was past practice; however, MTC corrected the payment process prior to the beginning of the Caltrans audit process.

The \$44,151 was retention inadequately billed to Caltrans. The retention was paid to the contractor (Check #90001188 – July 2009). As such, MTC respectfully requests the \$44,151 be reinstated.

Further, given that the payment practices were corrected long before the auditors arrived, the interest amount is not material and there have been no repeat instances. MTC requests that the concluding remarks that "... it would appear that the practice of billing the Department for consultant costs prior to incurring and paying the costs has been a standard practice of MTC ..." be removed.

Finding #3 (\$4,226,318):

MTC improperly awarded six consultant procurements for FSP.

We believe MTC appropriately followed its procurement practice. MTC's procurement award included review by the Office of General Counsel, approval of Executive Office and formal approval of the Commission. A full explanation is included under the attached Finding #3 information which includes the explanation of the Deputy Executive Director, as well as the relevant board memorandum of 2004 and 2005. MTC believes the procurements were properly conducted, evaluated and disclosed, and therefore, requests the comment be removed and all costs allowed.

Finding #4 (\$3,062,022):

Lack of adequate documentation to support consultant payments.

At the auditor's request, MTC produced over 600 checks and wires to support invoices. At the end of the field work, MTC staff believed they had provided all of the support requested by Caltrans. While we understand there were questions related to the records provided by the County of Alameda to support wire transfers from the Alameda account, we do not understand this as the basis for disallowing the expenses. MTC staff cannot force the County's investment pool to change their practice.

Nevertheless, we have pulled all of the support including obtaining wire copies directly from the County. As such, MTC requests that the finding be removed and the expenses allowed.

Finding #5 (\$1,312,171):

MTC incorrectly billed indirect and unallowable costs.

MTC staff disagrees in part and agrees in part, although the net result is immaterial to the overall amount covered by the audit. Our analysis indicates the final number is closer to \$100,000:

▪ Disallowed		<u>(\$1,312,171)</u>
▪ MTC staff believes there is a calculation error (detailed in red on schedule).	\$257,272	
▪ Graphics (W.E. #1154) is not a central reproduction shop but a specialized shop that overwhelmingly produces products and reports in direct support of the planning function and, as such, should remain a direct charge.	\$370,286	
▪ Computer Support (W.E. #1155) was billed directly as a result of their work developing record management systems and GIS projects in support of federal planning goals. Our analysis indicated ratio of directly chargeable project support to general system support was 65/35. (\$1,573,889 x .35)	\$550,859	
▪ Based on the letter from FHWA, the Executive Director of an MPO is not excluded from indirect costs under A-133. Since their letter is intended to clarify the issue, we propose to reinstate all Executive Director charges.	\$42,601	
▪ Net Adjustment	\$1,221,018	
▪ Balance of Disallowed Costs		<u>(\$ 91,153)</u>

While MTC staff concurs with the balance of the findings, we wish to remind Caltrans that all of the indirect costs, formulas and rates were all reviewed and approved by Caltrans.

Finding #6 (\$184,934):

Sub-recipient costs paid and billed 180 days after agreement termination.

MTC believes that project staff acted in accordance with verbal authorization from Caltrans project staff. MTC undertook this project at the request of Caltrans staff. Because of this request, Caltrans staff was aware that there were program delays that resulted in the delayed payments. This position is supported by the fact that Caltrans District staff approved our retaining the funds to make payments and accepted final report from MTC long after the grant was to close. MTC should not suffer harm for a project undertaken at the request of Caltrans and respectfully requests that the verbal agreement be honored with all costs allowed.

Finding #7:

Lack of accountability for advance.

MTC staff can concur that improved grant procedures are an excellent goal, but in this instance, MTC should not suffer harm for practices allowed by Caltrans staff. MTC undertook this project at the request of Caltrans local staff. In fact, from 2004 to 2007, MTC requested direction from MTC project and Caltrans staff on what to do with the funds remaining long after the grant was supposed to be closed. Because there were final delivery issues, Caltrans staff verbally directed MTC to retain funds, despite the fact the grant was never extended. Finally, without a request from Caltrans, MTC returned the unused balance to Caltrans.

MTC does not believe it is appropriate to make comments on our grant management capabilities when the actions were consistently authorized by Caltrans representatives. MTC undertook the program at the request of Caltrans and rather than be criticized for our actions, should instead be indemnified from adverse actions except in the case of fraud or illegal acts, of which there was none.

Finding #8 (\$222,533):

Final report of expenditures not reconciled.

\$83,023	MTC does not agree that \$83,023 was reclassified to maintain work element budgets and thus, should be allowed. MTC very carefully follows Caltrans relating to work elements budgets and in 2004/05, and Caltrans has provided no support that the budget for Work Element #1110 was ever exceeded in total. The audit is referring to internal program numbers that make up the detail for #1110 but are maintained for MTC's administrative and evaluation purposes only.
\$126,341	MTC concurs that this work item was over budget by error. However, the costs were allowable with funds remaining in the grant that, if we had properly amended the OWP, would have covered the expense. Since the expenses were allowable and repayment would be refunded by a future budget and, as such, no refund is necessary.
\$13,169	The charge was incorrectly posted and overdrew the account. However, the expense was allowable and there were funds remaining had the expense been properly posted.

MTC concurs that the \$126,341 and \$13,169 exceeded the adopted budgets but should be allowed as funds remained in the funding source and a refund would only be applied to future budgets. The \$83,023 is in error and should be allowed.

Finding #9:

Inappropriate billing practices.

Past practice at MTC has been to get the most out of project funding by charging most project management costs to local funding sources, not directly to the projects. MTC will review its staffing charges to verify that DOTP funding sources are not being inappropriately charged. Nevertheless, MTC is in the process of charging more project management costs directly against the grants.

Finding #10:

Inadequate Grant Management.

While we cannot completely concur with the finding, particularly in light of pulling over 600 checks and wires, as well as supporting information that dates back years. Further, after a detailed audit, there has been no finding of fraud, waste, abuse, illegal acts or expenditures that were not appropriate to the project or grant. MTC is working to improve its overall grant management program.

Finding #11:

Inadequate internal controls.

- Lack of proper invoice approval:

MTC has already corrected a past practice of allowing CMA invoices to be paid without signed approval and now include a copy of the signed approval sheets with Caltrans invoices. Current MTC practice is for all invoices to be approved by a project manager and section manager as part of the accounts payable process. All invoices to Caltrans are sent over the CFO's signature as signed certification that the expense has been properly incurred and paid.

- Inadequate control over access rights:

System access issues have been resolved and are now reviewed as part of closing controls.

- Signing invoices on behalf of the CFO:

The Senior Accountant was authorized to sign and approved invoices for the CFO in his absence, but signed his signature 'for' him. The individual's signature has now been signing 'for' the CFO.

- No Accounting Manual:

MTC is working to develop a procedures manual.

Finding #12:

Interagency agreements lack required provisions.

MTC has reviewed its agreements and believe they are generally in compliance although the attached memorandum indicates our legal office has some questions as to the specific of the finding.

Finding #13:

Consultant Contracts lack required fiscal provisions.

MTC has reviewed contract requirements and believes they are generally in compliance. However, additional wording will be added for clarity.

Finding #14:

Incorrect OWP descriptions.

MTC works each year to update language and remove outdated and inaccurate wording. MTC meets the annually with federal and state funding partners as part of the IPG review of the OPW. While no member of the IPG has specifically mentioned the OWP consists of outdated language, MTC works with its partners to produce an appropriately worded document.